ICRA

EXPECTATIONS

BUDGET 2024-25

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Agenda

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1 Government of India's fiscal performance in April-May 2024

2 Key Expectations for FY2025 Revised Budget

3 Expectations on Market Borrowings for FY2025

Highlights - I

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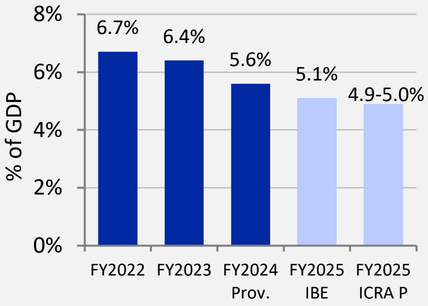
EXHIBIT: Fiscal deficit of the GoI



P: Projected; Source: Union Budget documents; CGA; ICRA Research

ICRA estimates the Government of India's (GoI's) revenue receipts to witness an upward revision of Rs. 1.2 trillion in the FY2025 Revised Budget over the Interim Budget Estimate (IBE), while pegging a relatively shallower increase in the revenue expenditure (revex) target, largely focused on the rural economy. The GoI is likely to set a fiscal deficit target at 4.9-5.0% for FY2025, vis-à-vis the IBE of 5.1% of GDP, without compromising the capital expenditure target of Rs. 11.1 trillion. Consequently, ICRA believes that there is a high likelihood of reducing the net market borrowings for FY2025 by Rs. 350-550 billion vis-à-vis the IBE of Rs. 11.8 trillion, which would augur well for yields, along with the demand boost for Government securities (G-secs) owing to their inclusion in the J.P. Morgan Government Bond Index. ICRA's analysis suggests that incremental fiscal consolidation will be challenging over the next 3-4 years. Moreover, the extent of off-budget capex 'on-budgeted' during FY2022-24 must be considered while assessing the end-point of the fresh medium-term fiscal glide path beyond FY2026.

- **Taxes and RBI dividend to provide additional leeway of Rs. 1.2 trillion on GoI's revenues:** The gross tax revenues in FY2024 Provisional estimates (Prov.) were Rs. 276 billion higher than the Revised Estimate (RE), which dampened the embedded growth target for FY2025 to 10.6%, lower than ICRA's nominal GDP forecast of 10.8% for the fiscal. Accordingly, ICRA believes that tax collections may be revised upwards by ~Rs. 400-450 billion in the Revised Budget Estimates (RBE) for FY2025. Consequently, ICRA conservatively pegs net tax revenues to exceed the IBE by ~Rs. 200 billion. Additionally, the larger-than-expected Reserve Bank of India (RBI) dividend would provide an upside of at least Rs. 1.0 trillion, leading to a sharp upward revision in estimates for non-tax revenues in the RBE vis-à-vis the IBE.
- **GoI likely to raise revex while maintaining capex at IBE levels:** Against the embedded growth target of 17.1% for FY2025 (over FY2024 Prov.), the GoI's capex declined by 14.4% YoY in April-May FY2025. Given this, and the typically low capex numbers in the monsoon months, the required monthly run-rate in H2 FY2025 would be quite sharp, making it challenging to achieve the IBE for the fiscal. Consequently, ICRA expects the GoI to retain its capex target of Rs. 11.1 trillion for FY2025. However, there is a distinct possibility of raising the budgeted target for revex

Highlights - II

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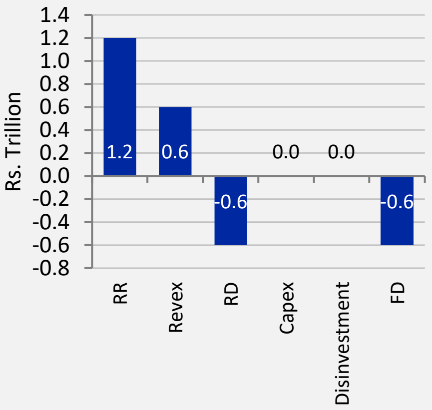
EXHIBIT: Variation in key fiscal metrices as per ICRA projections compared to IBE for FY2025



This entails a fiscal deficit target of 5.0% of GDP; RR: Net revenue receipts; RD: revenue deficit; FD: Fiscal deficit; Source: Union Budget documents; ICRA Research

compared to the IBE, either to introduce a new scheme or to increase the outlay for some existing schemes. ICRA estimates the GoI's revex to be raised by ~Rs. 500-600 billion vis-à-vis the IBE, representing a YoY growth of 6.0-6.3% (vs. 4.6% growth in FY2025 IBE over FY2024 prov.). The additional allocation is likely to be largely under the non-interest non-subsidy head, focused on the rural economy, given the tepid rural demand due to the spillovers of the inadequate and uneven monsoon of 2023.

- **GoI likely to target a fiscal deficit of 4.9-5.0% of GDP:** The incremental revenue receipts of Rs. 1.2 trillion can be split to increase the revenue spending and facilitate fiscal consolidation. An even split would aid in reducing the GoI's fiscal deficit to 5.0% of GDP in the full budget for FY2025 against the target of 5.1% of GDP mentioned in the IBE. ICRA believes that the GoI can scale back its fiscal deficit target to ~4.9-5.0% of GDP for FY2025.
- **Fiscal consolidation challenging beyond FY2025:** ICRA's projections indicate that reducing the absolute size of the fiscal deficit will be quite difficult over the next 3-4 years, with the decline in the fiscal deficit-to-GDP ratio largely dependent on the increase in nominal GDP. If the GoI continues with capex at 3.4% of GDP over the medium term (in line with the FY2025 IBE), then incremental fiscal consolidation would require a sustained compression in the revenue deficit. Notably, the GoI has 'on-budgeted' a large portion of previously off-budget capex; this should be considered while determining the endpoint of the awaited fresh fiscal consolidation roadmap beyond FY2026. Assuming that capex of ~1.0% of GDP has been brought on budget, the GoI could consider further reducing its fiscal deficit target to 4.0% of GDP over the medium term, from the expected sub-4.5% of GDP in FY2026.
- **H2 FY2025 borrowings likely to be cut by Rs. 350-550 billion:** The Centre is likely to temper down its borrowing compared to the amount pencilled in the IBE, depending on the magnitude of reduction in the fiscal deficit number. Based on ICRA's expectations of a smaller-than-budgeted fiscal deficit at 4.9-5.0% of GDP for FY2025, the Centre's gross and net market issuances can be reduced by Rs. 350-550 billion for H2 FY2025, thereby auguring well for G-sec yields, along with the demand boost for G-secs owing to the bond index inclusion.

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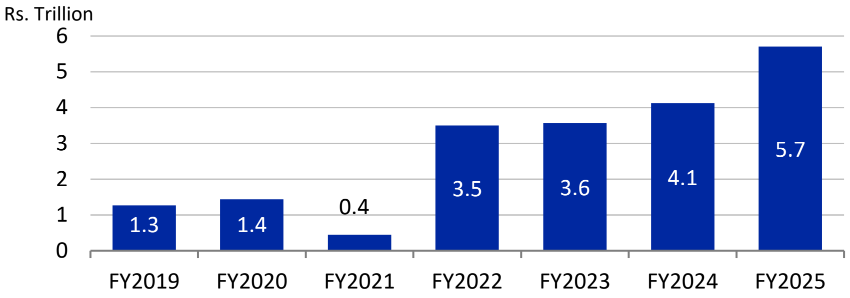
GOI's FISCAL PERFORMANCE IN APRIL-MAY 2024

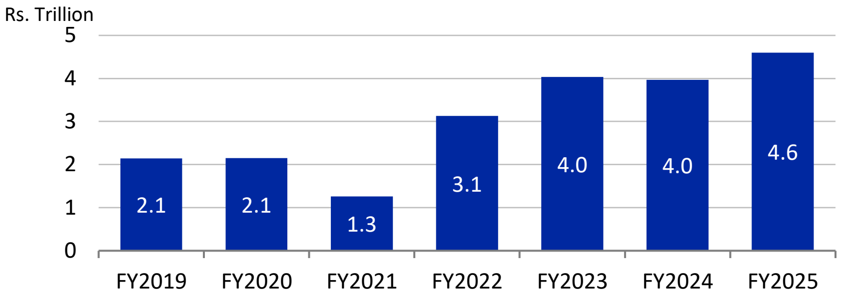
Revenue receipts rose sharply by ~38% during April-May 2024

EXHIBIT: Revenue receipts in April-May of FY2019-25



Source: CGA, Ministry of Finance, GoI; ICRA Research

EXHIBIT: Gross tax revenues in April-May of FY2019-25

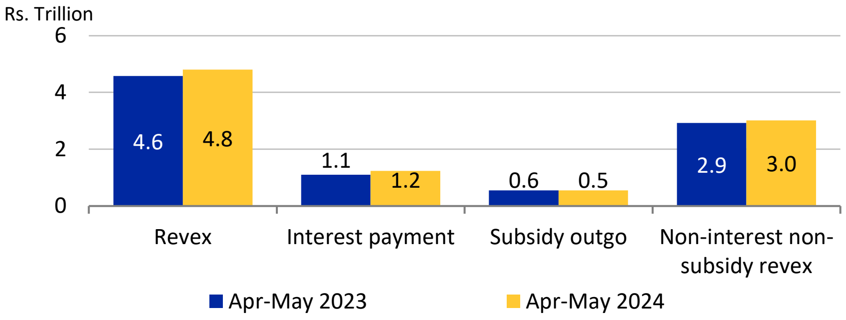


Source: CGA, Ministry of Finance, GoI; ICRA Research

- The provisional data indicates that the GoI's revenue receipts rose sharply by 38.3% to Rs. 5.7 trillion (19.0% of FY2025 BE) during April-May 2024 from Rs. 4.1 trillion during April-May 2023 (15.1% of FY2024 Prov.). This increase was driven by non-tax revenues (nearly doubling to Rs. 2.5 trillion from Rs. 1.3 trillion; 63.0% of FY2025 BE) and net tax revenues (+14.7%; to Rs. 3.2 trillion from Rs. 2.8 trillion; 12.3% of FY2025 BE).
- The GoI's gross tax revenues rose by a healthy 15.8% YoY to Rs. 4.6 trillion during April-May 2024 (12.0% of FY2025 BE) from Rs. 4.0 trillion during April-May 2023 (11.5% of FY2024 Prov.), led by a robust uptick in direct taxes (+22.7%; to Rs. 2.3 trillion during April-May 2024 from Rs. 1.8 trillion during April-May 2023), followed by a relatively lower rise in indirect taxes (+7.5%; to Rs. 2.0 trillion from Rs. 1.9 trillion).
- The sharp uptick in direct taxes in April-May 2024 was entirely driven by income tax collections (YoY: +41.6%), even as corporation tax (-19.8%) declined sharply during this period. Additionally, within indirect taxes, the YoY increase in collections from CGST (+12.2%) and customs duty (+3.8%) was partly offset by the contraction in union excise duty collections (-5.8%) during April-May 2024.

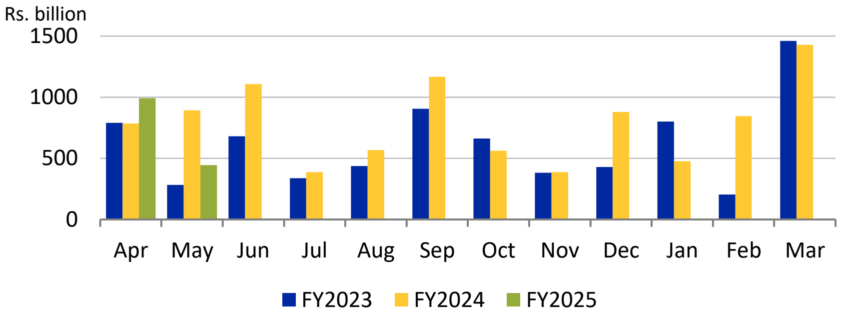
GoI's capex declined during April-May 2024, amid Model Code of Conduct for General Elections; revex rose by ~5%

EXHIBIT: Monthly trends in revenue expenditure and its components



Source: CGA, Ministry of Finance, GoI; ICRA Research

EXHIBIT: Monthly Trends in Gross Capital Expenditure



Source: CGA, Ministry of Finance, GoI; ICRA Research

- The GoI's total expenditure decreased by 0.4% YoY to Rs. 6.2 trillion during April-May 2024 (13.1% of FY2025 BE) from Rs. 6.3 trillion during April-May 2023 (14.1% of FY2024 Prov.), amid the prevailing Model Code of Conduct for the Parliamentary Elections.
- This was driven by a 14.4% decline in capex, to Rs. 1.4 trillion during April-May 2024 (12.9% of FY2025 BE) from Rs. 1.7 trillion during April-May 2023 (17.7% of FY2024 Prov.), with the monthly capex halving to Rs. 443.9 billion in May 2024 from Rs. 893.3 billion in May 2023 (Rs. 992.4 billion in April 2024).
- In contrast, revex had risen by 4.7% during April-May 2024 (to Rs. 4.8 trillion from Rs. 4.6 trillion) led by interest payments (YoY: +11.9%), even as outgo towards major subsidies eased (-1.1%). The subsidy outlay for fertilisers (-34.6%; to Rs. 160.3 billion during April-May 2024 from Rs. 245.1 billion during April-May 2023) declined, while that for food (+25.1%; to Rs. 385.4 billion from Rs. 308.1 billion) and fuel (to Rs. 122.5 billion vs. nil) rose during April-May 2024.
- The non-interest non-subsidy revex expanded by a relatively lower 3.1% YoY to Rs. 3.0 trillion during April-May 2024 from Rs. 2.9 trillion during April-May 2023. Monthly revex dipped to Rs. 1.6 trillion in May 2024 from Rs. 2.3 trillion in May 2023 (Rs. 3.2 trillion in April 2024).

Higher-than-budgeted RBI dividend transfer, decline in spending led to revenue and fiscal surplus in May 2024

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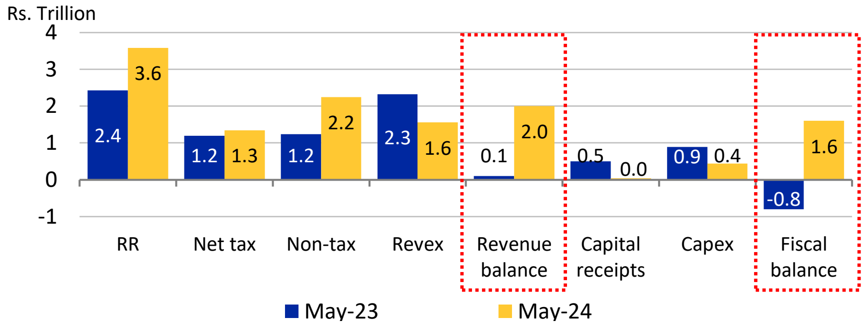
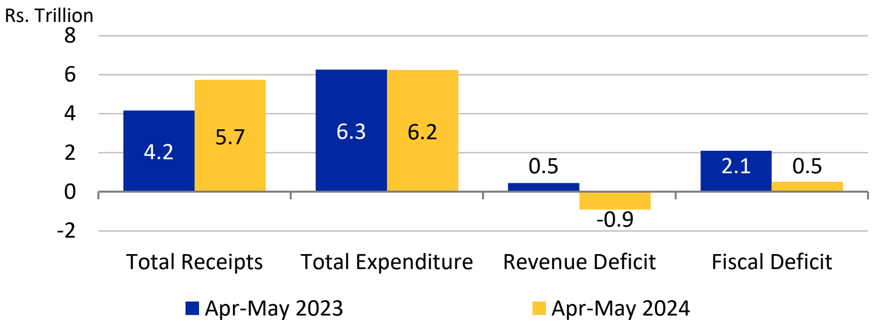
EXHIBIT: GoI's revenue and expenditure trends in May 2023 and 2024



Source: CGA, Ministry of Finance, GoI; ICRA Research

EXHIBIT: Trends in Revenues and Expenditure of the GoI during Apr-May 2023 and 2024



Source: CGA, Ministry of Finance, GoI; ICRA Research

- In May 2024, the GoI's revenue receipts rose by ~48% with a surge in non-tax revenues (YoY: +81.4%; owing to an expectedly large RBI dividend transfer of Rs. 2.1 trillion). This, along with the 33.1% YoY fall in revex, led to a revenue surplus of Rs. 2.0 trillion in May 2024, higher than Rs. 0.1 trillion for May 2023.
- Additionally, the GoI recorded a fiscal surplus of Rs. 1.6 trillion for May 2024 with the capex halving in May 2024 amid the Model Code of Conduct for the General Elections, in contrast to the deficit of Rs. 0.8 trillion witnessed in May 2023.
- Overall, with revenue receipts (Rs. 5.7 trillion; YoY: +38.3%) exceeding revenue spending (Rs. 4.8 trillion; +4.7%) during April-May 2024, the GoI witnessed a revenue surplus of Rs. 0.9 trillion during that period, as opposed to the deficit of Rs. 0.5 trillion observed during April-May 2023. Further, with a decline in the capex (-14.4%), the GoI's fiscal deficit was curtailed at Rs. 0.5 trillion (3.0% of FY2025 BE), relative to Rs. 2.1 trillion (12.7% of FY2024 Prov.).

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KEY EXPECTATIONS FOR FY2025 REVISED BUDGET

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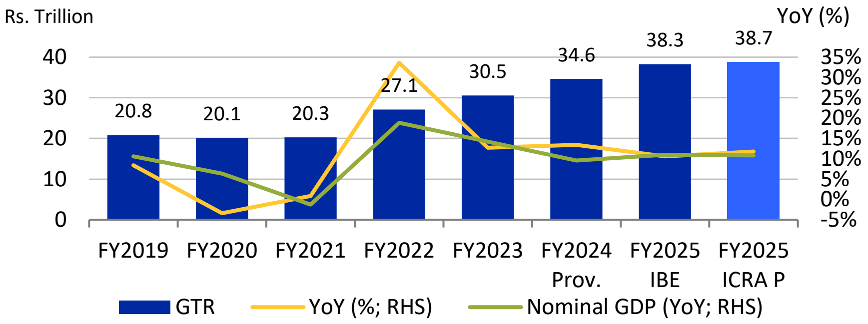
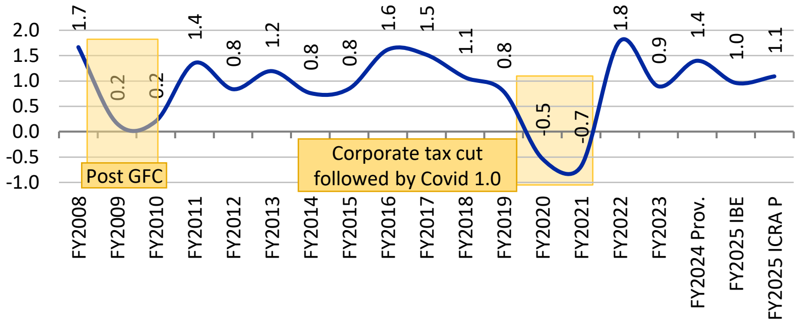
Gross tax revenues likely to be raised by ~Rs. 400-450 billion in FY2025 RBE vs. IBE, assuming a tax buoyancy of 1.1

EXHIBIT: Trends in GoI's Gross Tax Revenues and nominal GDP



Prov: Provisional; IBE: Interim Budget Estimate; P: Projected; Source: GoI Budget Documents; CGA; NSO; ICRA Research

EXHIBIT: Tax Buoyancy of the GoI

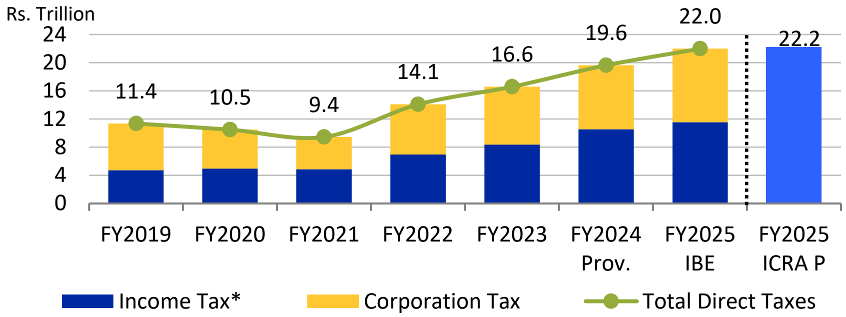


Tax buoyancy is a proportion of % change in Gross tax revenues and % change in Nominal GDP growth; Source: Union Budget; CGA; NSO; ICRA Research

- The GoI had pegged its gross tax revenues (GTR) at Rs. 38.3 trillion in the FY2025 IBE, entailing an expansion of 11.5% over FY2024 RE. However, as per the provisional estimates for FY2024, such revenues exceeded the RE by Rs. 275.8 billion (Prov.: 34.6 trillion vs. RE: Rs. 34.4 trillion). This overshooting implies that the embedded growth target for FY2025 is now pegged at a shallower 10.6% than that included earlier in the IBE. This is mildly lower than our nominal GDP projection of 10.8% in FY2025, and implies a tax buoyancy of 1.0, which is lower than the historical average.
- **ICRA believes that the gross tax revenues may be revised upwards by ~Rs. 400-450 billion in the RBE for FY2025, from Rs. 38.3 trillion estimated in the Interim Budget, translating to a YoY growth of 11.8% over the FY2024 Prov.**
- With the growth in GTR (YoY: +13.4%) sharply exceeding that in the nominal GDP (+9.6%), the tax buoyancy printed at 1.4 in FY2024 Prov. **We have assumed a buoyancy of 1.1 while projecting the GTR for FY2025, slightly higher than 1.0 estimated in FY2025 IBE, albeit in line with the historical average seen during FY2014-19.**

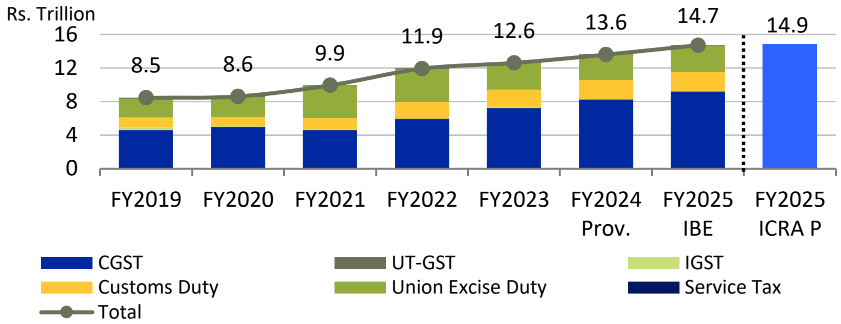
Direct and indirect taxes projected to be revised upwards in FY2025 RBE vs. IBE

EXHIBIT: Trends in direct taxes



Including other taxes such as fringe benefit tax, securities transaction tax, etc.; Prov.: Provisional; IBE: Interim Budget Estimates; P: Projected; Source: CGA, Ministry of Finance, GoI; ICRA Research

EXHIBIT: Trends in indirect taxes

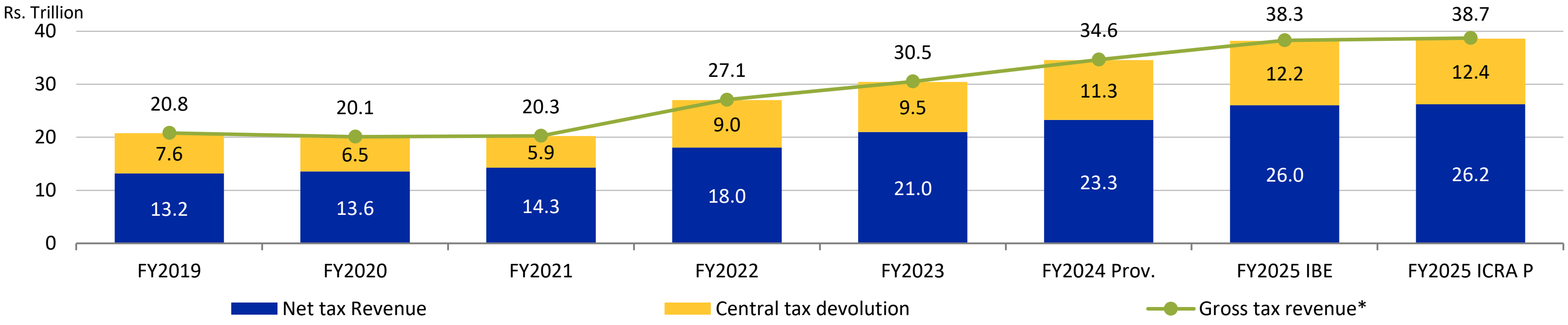


Prov.: Provisional; IBE: Interim Budget Estimates; P: Projected; Source: CGA, Ministry of Finance, GoI; ICRA Research

- The GoI had estimated direct tax collections at Rs. 22.0 trillion in the FY2025 IBE, entailing a YoY growth of 13.1% over FY2024 RE. However, the FY2024 Prov. for these collections exceeded the RE by Rs. 189.1 billion (Prov.: Rs. 19.6 trillion vs. RE: Rs. 19.5 trillion), driven by income tax collections* (+Rs. 305.3 billion). Consequently, the YoY growth target for FY2025 now stands at 12.0%, lower than the IBE. **Based on this, ICRA expects the direct taxes to be raised by ~Rs. 200 billion in the FY2025 RBE from Rs. 22.0 trillion estimated in the IBE, thereby translating to a YoY growth of 13.0% over FY2024 Prov., similar to the IBE target.**
- Similarly, the indirect tax collections were projected at Rs. 14.7 trillion in FY2025 IBE, with a YoY growth of 10.0% over FY2024 RE. Moreover, such receipts exceeded the FY2024 RE by Rs. 207.4 billion in the FY2024 Prov. (Prov.: Rs. 13.6 trillion vs. RE: Rs. 13.4 trillion), largely driven by higher collections from customs duty (+Rs. 143.9 billion) and CGST (+Rs. 90.2 billion). This translates to a YoY growth of 8.3% embedded for FY2025, slightly lower than the IBE. **ICRA believes that the indirect tax collections may be revised upwards by ~Rs. 150 billion, with the embedded growth target in the FY2025 RBE (ICRA's exp.: +9.5%) remaining largely similar to that budgeted initially in the IBE (+10.0%).**

Upward revision in GTR to push up tax devolution to states and net tax revenues by Rs. 200 billion each in FY2025 RBE

EXHIBIT: Trends in Central tax devolution, Centre's Gross and Net tax revenues



**Including transfers to NDRF/NCCF; Actuals for FY2019-23; P: Projected; IBE: Interim Budget Estimates; Prov.: Provisional; Source: Union Budget Documents, GoI; CGA; ICRA Research*

- The 15th Finance Commission had recommended the share of states in the shareable Central taxes (or central tax devolution; CTD) at 41% for its award period of FY2022 to FY2026. However, the effective rate of devolution, relative to the gross tax revenues of the GoI, tends to be closer to 30-33%, as cesses and surcharges are not included in the shareable pool.
- **Given our estimates for gross tax revenues for FY2025 RBE and the effective rate of devolution, ICRA estimates the tax devolution to the states to be raised by ~Rs. 200 billion from Rs. 12.2 trillion, estimated in the Interim Budget for FY2025. This entails a growth of 9.7% over FY2024 Prov., lower than the 11.8% growth projected for gross tax revenues**, given that the latter includes some growth in cesses and surcharge components (namely cess on petroleum products, health and education, as well as surcharge on direct taxes) for FY2025. Notably, the FY2024 Prov. for the CTD was higher than the RE by Rs. 250 billion.
- **After the CTD adjustment, ICRA projects the GoI's net tax revenues to be revised upwards by ~Rs. 200 billion from Rs. 26.0 trillion estimated in the FY2025 IBE, translating to a YoY expansion of 12.8% (+11.8% in IBE vs. FY2024 Prov.).**

GoI's non-tax revenues to be raised by ~Rs. 1.0 trillion in FY2025 RBE on account of higher RBI dividend transfer; disinvestment target unlikely to be changed

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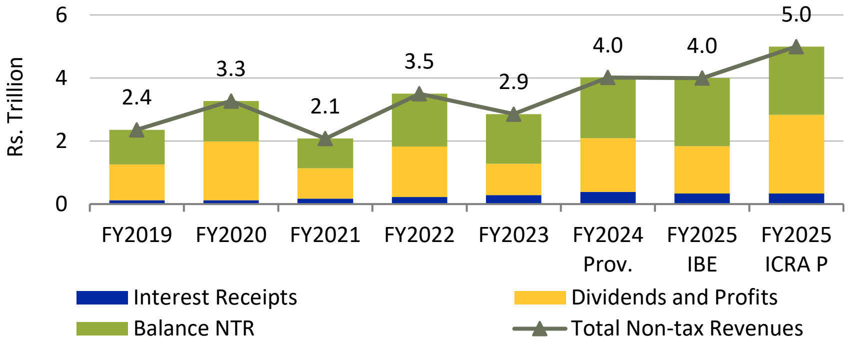
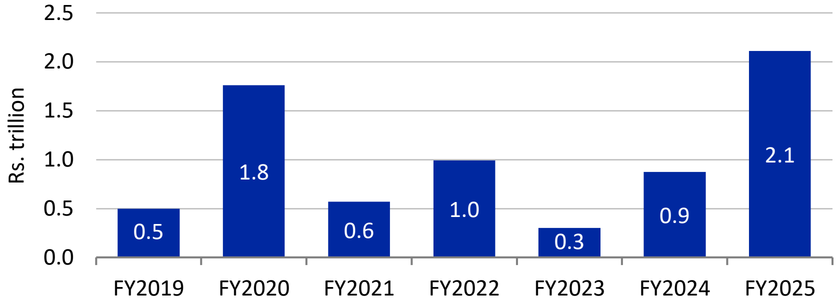
EXHIBIT: Non-tax revenues and components



P: Projected; Source: RBI; ICRA Research

EXHIBIT: Trends in RBI's surplus transfer to the GoI



Source: RBI; ICRA Research

- The GoI had estimated its non-tax revenues at Rs. 3.99 trillion in FY2025 IBE, a marginal 0.5% lower than Rs. 4.01 trillion in FY2024 Prov.
- Subsequently, on May 22, 2024, the RBI announced a dividend pay-out of Rs. 2.11 trillion to the GoI in FY2025 (the highest till date; Rs. 0.9 trillion in FY2024), more than double the amount transferred in the previous fiscal, stemming from a steep YoY fall of 56.3% in RBI's expenditure in FY2024 combined with a robust growth of 31.8% in the interest income. This amount is well above the Rs. 1.02 trillion budgeted for the dividends from the RBI, nationalised banks and FIs for FY2025. **Based on this, ICRA expects the GoI's non-tax revenue target for FY2025 to be revised upwards by Rs. 1.0 trillion to Rs. 5.0 trillion in the final Budget estimates from Rs. 4.0 trillion in the IBE, translating to a robust YoY growth of 24.3% over the FY2024 Prov.**
- Moreover, the GoI's disinvestment proceeds were pegged at Rs. 500 billion in FY2025 IBE (Rs. 171.5 billion in FY2024 Prov.). According to data provided by the DIPAM, disinvestment receipts have remained nil in FY2025 so far (up to July 5, 2024). **ICRA believes that the GoI is unlikely to revise its disinvestment target for FY2025 at the current juncture.**

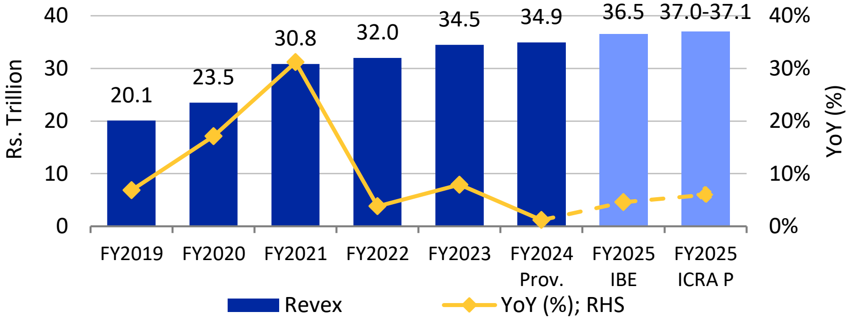
Revenue expenditure target expected to be raised by Rs. 0.5-0.6 trillion in FY2025 compared to the IBE …

EXHIBIT: Revex and major heads

Rs. Trillion	FY2024 RE (A)	FY2024 Prov. (B)	FY2025 IBE (C)	C/A	FY2025 ICRA P (D)	D/B
Revex	35.4	34.9	36.5	**3.2%**	37.0-37.1	**6.0-6.3%**
Interest outgo	10.6	10.6	11.9	**12.8%**	12.0	**12.8%**
Aggregate Subsidy (food, fertiliser and fuel)	4.1	4.1	3.8	**-7.8%**	3.8	**-7.8%**
Balance Revex*	20.7	20.2	20.8	**0.6%**	21.2-21.3	**5.2-5.8%**

**Total revex minus interest payments and aggregate subsidy outgo; P: Projected; Source: GoI Budget Documents; CGA; Ministry of Finance, GoI; ICRA Research*

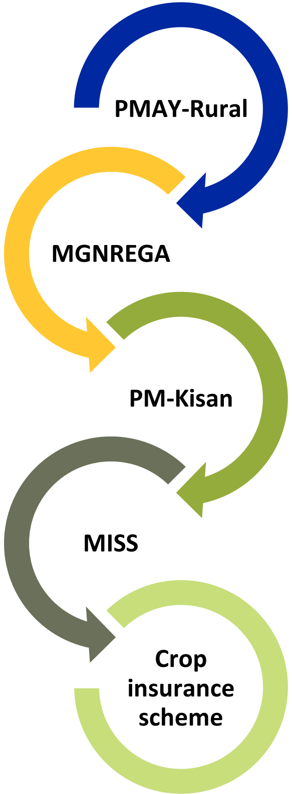
EXHIBIT: Annual trends in revenue expenditure

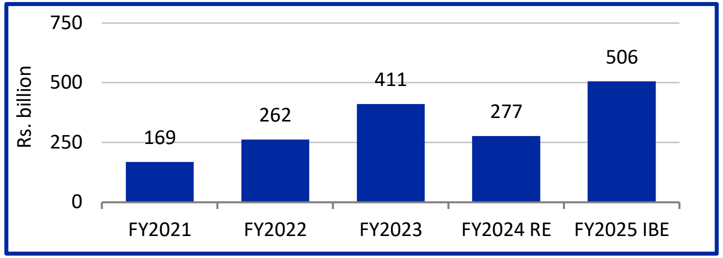


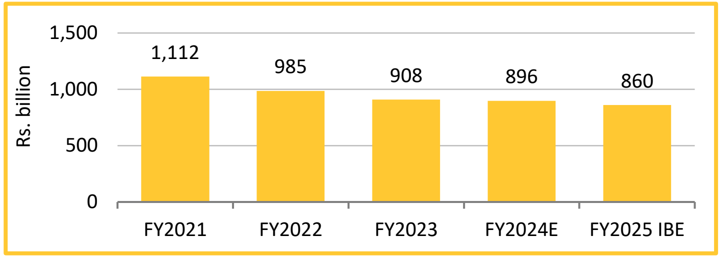
Actuals for FY2019-23; Prov: Provisional; IBE: Interim Budget Estimates; P: Projected; Source: CGA, Ministry of Finance, GoI; ICRA Research

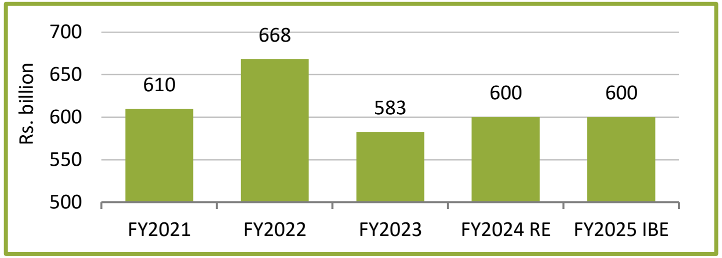
- With revenue expenditure in FY2024 Prov. (Rs. 34.9 trillion) being lower than the revised target (Rs. 35.4 trillion), the embedded budgeted growth under this head for FY2025 IBE turns out to be slightly higher at 4.6%, against 3.2% growth indicated for the fiscal over FY2024 RE.
- The YoY trends were volatile for revex in the first two months of FY2025, with a 43.7% surge in April 2024 followed by a sharp 33.1% contraction in May 2024. Overall, the revenue expenditure increased by a modest 4.7% to Rs. 4.8 trillion in April-May FY2025 from Rs. 4.6 trillion in the year-ago period.
- There is a possibility of raising the budgeted target for revex compared to the IBE, either to bring in a new scheme or to increase the outlay for some of the existing schemes. **ICRA estimates the GoI's revenue expenditure at Rs. 37.0-37.1 trillion, Rs. 500-600 billion higher than the IBE, representing a YoY growth of 6.0-6.3%. The additional allocation is largely likely to be under the non-interest non-subsidy head, focused on rural economy, given the tepid rural demand owing to the spillovers of the inadequate and uneven monsoon seen in 2023.**

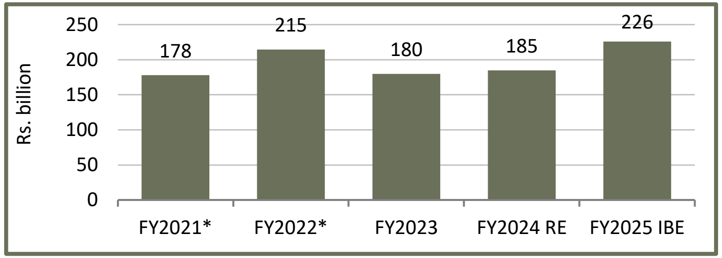
… likely to be rural-focussed, with a higher allocation for existing schemes or introduction of new schemes

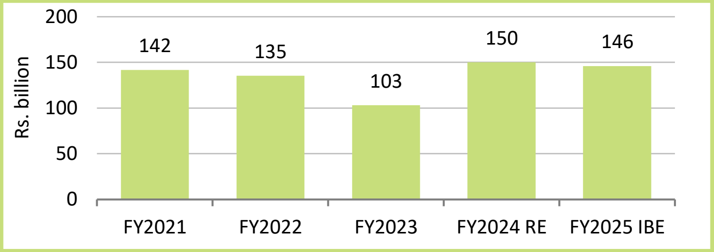








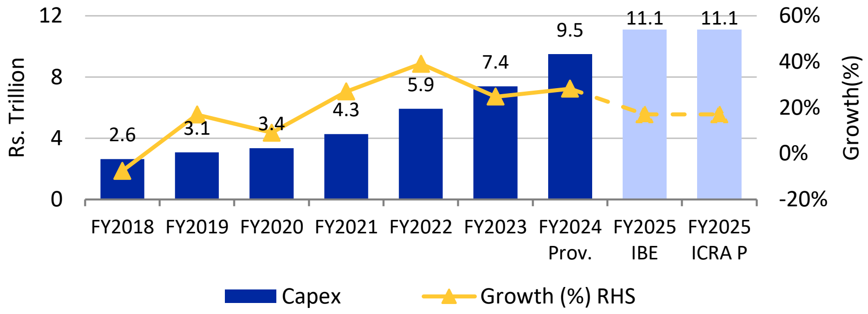




*includes allocation for the erstwhile interest subsidy for short term credit to farmers, which later was revamped to Modified Interest Subvention Scheme (MISS); Source: Union Budget; ICRA Research

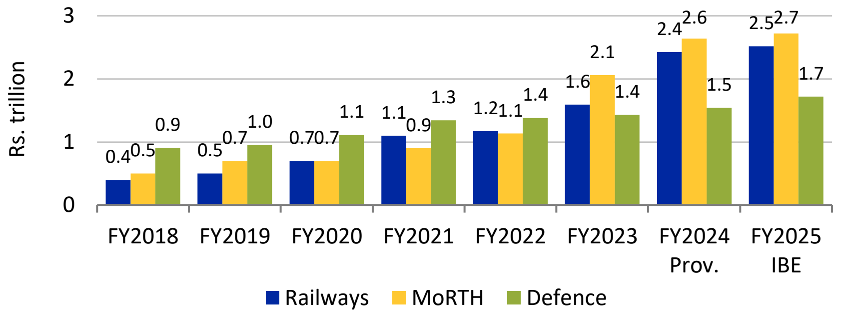
Capex target of Rs. 11.1 trillion likely to be retained in FY2025, amid sluggish trend in early months

EXHIBIT: Trends in GoI's Gross Capital Expenditure



Actuals for FY2018-23; P: Projected; Source: GoI Budget Documents; CGA; Ministry of Finance, GoI; ICRA Research

EXHIBIT: Trends in GoI's capital expenditure towards major sectors



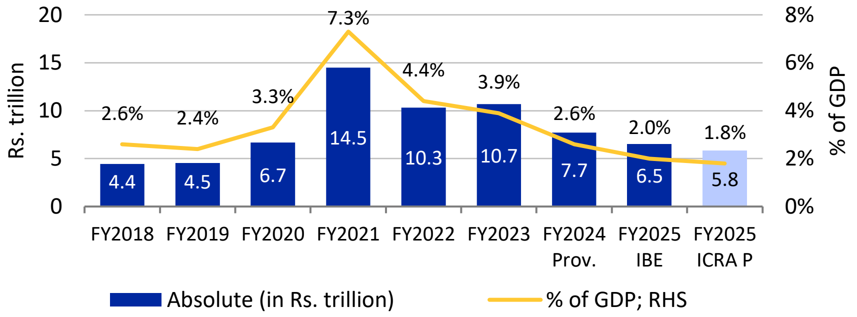
Actuals for FY2018-23; Source: GoI Budget Documents; CGA; Ministry of Finance, GoI; ICRA Research

- Against the embedded growth target of 17.1% (at Rs. 11.1 trillion) for FY2025 (over FY2024 Prov.), the GoI's capital expenditure moderated by 14.4% on a YoY basis to Rs. 1.4 trillion in April-May FY2025 amid a volatile monthly trend. After surging by 26.5% YoY to Rs. 1.0 trillion in April 2024, possibly attributable to the early release of funds prior to the onset of Parliamentary Elections, the capex plunged by 50% YoY and 55% MoM to Rs. 0.4 trillion in May 2024.
- Moreover, the capex numbers are typically low in the monsoon months, thereby suggesting that the required monthly run rate in H2 FY2025 would be quite sharp. This would make it challenging to even achieve the IBE for the fiscal. Consequently, ICRA believes that the GoI is likely to retain its capital expenditure target of Rs. 11.1 trillion for FY2025.
- Besides, the GoI had allocated a fairly large capex amounting to Rs. 0.7 trillion for 'new schemes' under the Finance Ministry allocations in the FY2025 IBE, which accounts for a bulk of the Rs. 1.6 trillion expansion in the aggregate capex over the FY2024 levels. With the details of this scheme not provided, this is likely to have been a placeholder entry to show a double-digit expansion in the capex in the IBE. This amount is now likely to be distributed between the various ministries, thereby enhancing their respective capex numbers, while keeping the aggregate number unchanged.

Fiscal deficit target for FY2025 likely to be scaled back to 4.9-5.0% of GDP vis-à-vis 5.1% indicated in IBE

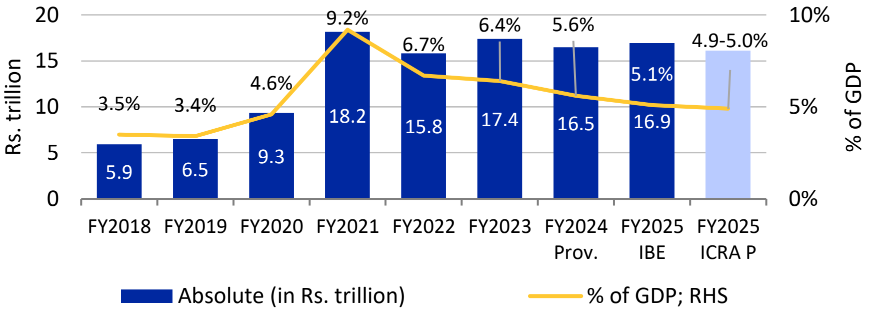
ICRA

EXHIBIT: GoI's Revenue Deficit (Absolute and % of GDP)



Actuals for FY2018-23; P: Projected; Source: GoI Budget Documents; CGA; Ministry of Finance, GoI; ICRA Research

EXHIBIT: GoI's Fiscal Deficit (Absolute and % of GDP)

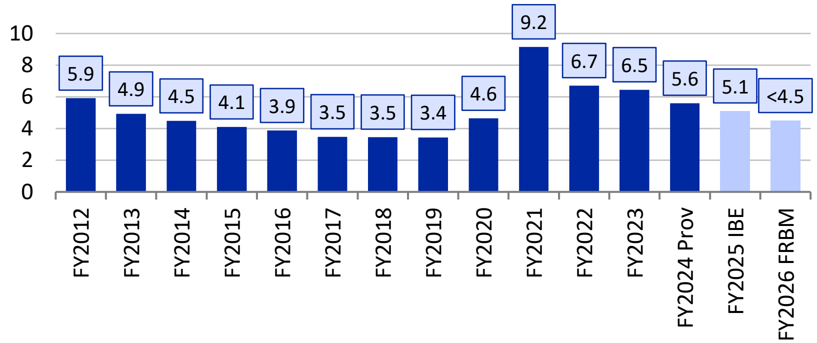


Actuals for FY2018-23; P: Projected; Source: GoI Budget Documents; CGA; Ministry of Finance, GoI; ICRA Research

- Given the large upside stemming from the RBI dividend, ICRA believes that the revenue deficit target for FY2025 can certainly be curtailed vis-à-vis that included in the IBE (Rs. 6.5 trillion; 2.0% of GDP), unless the revenue expenditure target is increased by an unexpectedly large amount.
- The incremental revenue receipts of Rs. 1.2 trillion can be split for raising the revenue spending and facilitating the fiscal consolidation. An even split would help reduce the GoI's fiscal deficit to 5.0% of GDP in the full budget for FY2025 against the target of 5.1% of the GDP mentioned in the IBE.
- **Overall, ICRA believes that the GoI can scale back its fiscal deficit target to ~4.9-5.0% of GDP for FY2025, without sacrificing the capex target of Rs. 11.1 trillion.**

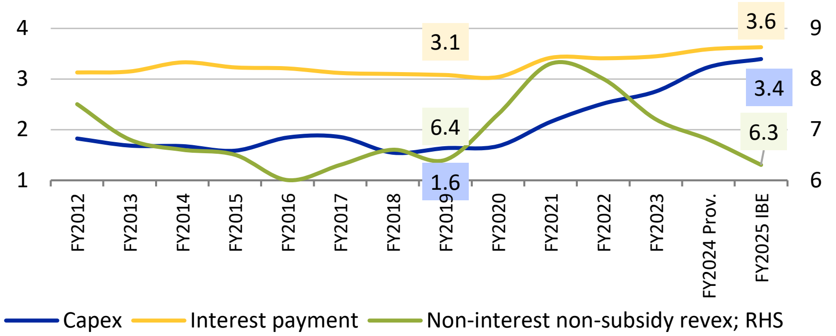
Fiscal consolidation to turn challenging beyond FY2025

EXHIBIT: Centre's fiscal deficit to GDP ratio (%)



IBE: Interim Budget Estimate; Source: Union Budget; CGA; ICRA Research

EXHIBIT: Capex, interest payments, non-interest non-subsidy revex (% of GDP)



Actuals for FY2018-23; Prov: Provisional; Source: GoI Budget Documents; CGA; Ministry of Finance, GoI; ICRA Research

- The GoI had stopped publishing pre-fixed rolling targets for fiscal consolidation from the FY2022 Budget and had instead provided a broad fiscal glide path of reaching sub-4.5% deficit by FY2026, as per the FY2025 statement of fiscal policy under FRBM Act, 2003. It may very well continue with a broad glide path, without specifying the annual targets, amidst the ongoing geopolitical uncertainties. However, the endpoint of this medium-term glide path would be crucial to assess the GoI's intent to continue with fiscal consolidation, and also to determine the potential trajectory of the Government's debt-to-GDP ratio.
- **While favourable developments on the revenue front portend positively for the fiscal dynamics in FY2025, ICRA believes that fiscal consolidation will turn quite challenging beyond the current fiscal. As per our projections, reduction of the absolute size of the fiscal deficit will be quite difficult over the next three to four years and the decline in the fiscal deficit-to-GDP ratio will largely be determined by the increase in nominal GDP.**
- **If the GoI continues with a capex number at 3.4% of GDP over the medium term, similar to that pencilled in the FY2025 IBE, this would imply that incremental fiscal consolidation would entail a sustained compression in the revenue deficit.** This seems quite challenging, given the rising ratio of interest payments to GDP, even as non-interest non-subsidy revex has been budgeted to curtail to 6.3% of GDP, similar to pre-Covid levels of FY2019, after witnessing a surge in the Covid years.

Extent of 'on-budgeting' of previously off-budget capex must be given due consideration while assessing end-point of medium-term fiscal consolidation

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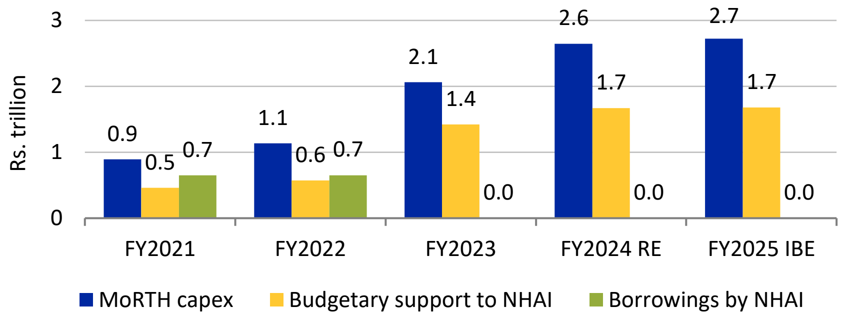
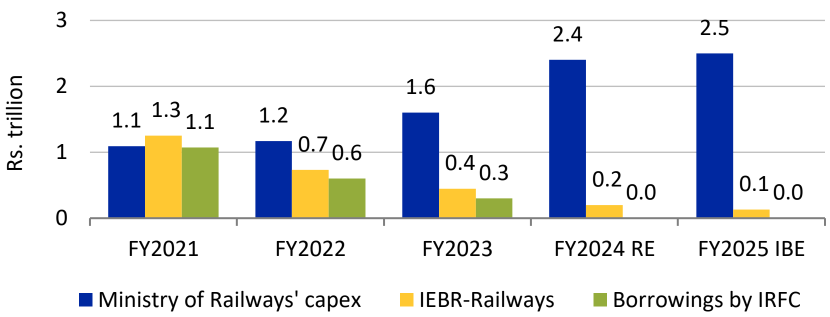
EXHIBIT: Capex by MoRTH, Budgetary support to NHAI and borrowings by NHAI



IBE: Interim Budget Estimate; Source: Union Budget; CGA; ICRA Research

EXHIBIT: Capex by Ministry of Railways, IEBR-Railways and borrowings by IRFC



IBE: Interim Budget Estimate; Source: Union Budget; CGA; ICRA Research

- Notably, the GoI has brought a large amount of off-budget capex onto its budget over the last three years. For instance, the Ministry of Road Transport and Highways' capex was raised sharply to Rs. 2.1 trillion in FY2023 from Rs. 1.1 trillion in FY2022, owing to a Rs. 0.8 trillion increase in the budgetary support to the National Highways Authority of India (NHAI) between these years, while the borrowing by the agency was cut to nil during FY2024 RE-FY2025 IBE from Rs. 0.7 trillion, to prevent a further build-up of debt. Likewise, the Railway Ministry's capex has expanded at a rapid pace during FY2022-24, even as Indian Railway Finance Corporation's (IRFC) borrowings were slashed to nil from Rs. 0.6 trillion between these years.
- **This 'on-budgeting' of the previously off-budget capex has been partly responsible for pushing up the Centre's gross capex to 3.4% of GDP in the IBE for FY2025 from 2.1% of GDP in FY2021. ICRA believes that this should be given due consideration while determining the end point of the awaited fresh fiscal consolidation roadmap over the medium term. Presuming that capex of around 1.0% of the GDP has been brought on budget, the GoI could consider further paring its fiscal deficit target to 4.0% of the GDP over the medium term, from the expected sub-4.5% of the GDP in FY2026.**

EXPECTATIONS ON MARKET BORROWINGS FOR FY2025

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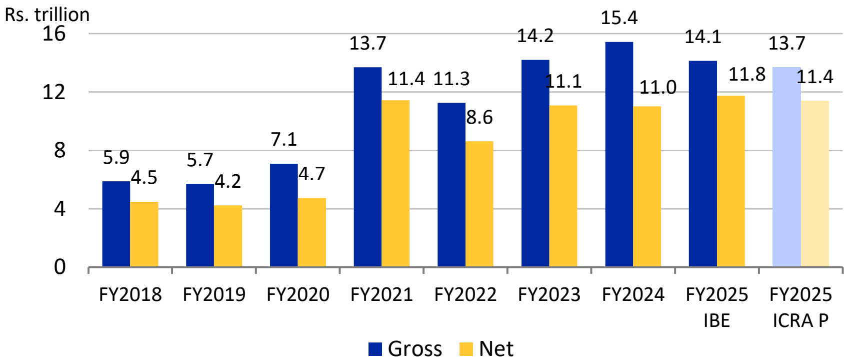
FY2025 market borrowings can be curtailed by Rs. 350-550 billion

EXHIBIT: Trends in GoI's gross and net market borrowings



Note: Actuals till FY2024; IBE: Interim Budget Estimate; Source: RBI; Union Budget; ICRA Research

EXHIBIT: Progress of market issuances in FY2025

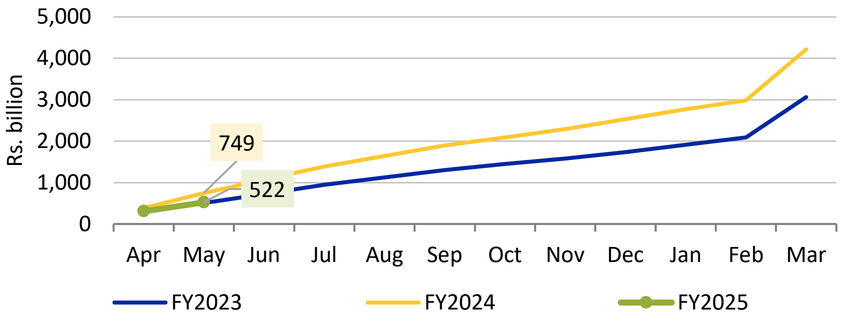
Rs. Trillion	FY2024	FY2025	Growth
Gross Borrowings - Planned	15.4	14.1	-8.4%
Gross Borrowings Completed*	4.8	4.0	-16.7%
% of Gross Borrowings completed	31.1%	28.3%	
Devolvement*	0.00	0.00	
Cancellations*	0.00	0.06	
Redemptions	3.6	2.4	-34.4%
Redemptions*	1.6	1.1	-32.1%
Net Borrowings	11.80	11.75	-0.4%
Net Borrowings Completed*	3.2	2.9	-9.1%
% of Net Borrowings completed	27.2%	24.9%	

**FY2025: Up to July 5, 2024, and for FY2024: up to July 7, 2023; Source: GoI; RBI; ICRA Research*

- The GoI had budgeted gross and net market issuances at Rs. 14.1 trillion and Rs. 11.8 trillion, respectively, for FY2025 in its IBE, entailing a YoY decline of 8.4% and 0.4% over the actual issuances of FY2024. Up to July 5, 2024, gross and net market issuances moderated by 16.7% and 9.1% in YoY terms.
- However, there is a possibility that the Centre can temper down its borrowing numbers compared to what was pencilled in the IBE, depending upon the magnitude of reduction in the fiscal deficit number, compared to Rs. 16.9 trillion or 5.1% of GDP included in the IBE.
- **Based on our expectations of a smaller-than-budgeted fiscal deficit at 4.9-5.0% of GDP for FY2025, Centre's gross and net market issuances can be reduced by Rs. 350-550 billion for H2 FY2025, thereby auguring well for G-sec yields, along with the demand boost for G-secs owing to the bond index inclusion.**

Interim budget target for small savings schemes of Rs. 4.66 trillion likely to be retained for FY2025

EXHIBIT: Cumulative inflows in saving deposits and certificates, and PPF



Source: CGA; ICRA Research

EXHIBIT: Interest rates on various Small Savings Schemes

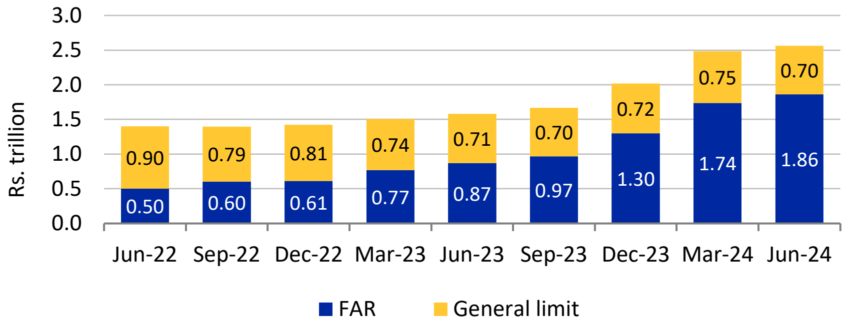
	Q1 and Q2 FY2025
Savings Deposit	4.0%
1-year Time Deposit	6.9%
2-year Time Deposit	7.0%
3-year Time Deposit	7.1%
5-year Time Deposit	7.5%
5-year Recurring Deposit	6.7%
5-year Senior Citizens Saving Scheme	8.2%
5-year Monthly Income Scheme	7.4%
5-year National Savings Certificate	7.7%
Public Provident Fund	7.1%
Kisan Vikas Patra	7.5%
Sukanya Samriddhi Account Scheme	8.2%

Source: DEA; ICRA Research

- In the Interim Budget, the GoI had mildly pared the net amount from small savings to fund its fiscal deficit to Rs. 4.66 trillion in FY2025 IBE from Rs. 4.71 trillion in FY2024 RE. Nearly 96% of the latter or Rs. 4.51 trillion was garnered as per the provisional data released subsequently by the CGA for FY2024.
- The cumulative inflows under savings deposit and certificates, and PPF increased by an impressive 37.5% YoY to Rs. 4.2 trillion in FY2024 Prov. (97% of FY2024 RE of Rs. 4.7 trillion) from Rs. 3.1 trillion in FY2023, benefitting from the upward revision of 20-90 bps in interest rates on small savings schemes through FY2024 and the uptick in spreads of several schemes over comparable G-sec yields through the year, as well as increase in the deposit limits for some schemes.
- In April-May FY2025, such inflows moderated by ~30% on a YoY basis amounting to Rs. 0.5 trillion, compared to Rs. 0.7 trillion garnered in 2M FY2024, which can be partly attributed to the heatwave conditions and consequent impact on the ability of households to deposit funds. This trend is likely to reverse given the favourable spreads for Q2 FY2025, even as rates for all schemes were kept unchanged at Q1 FY2025 levels. The GoI may retain the IBE target for FY2025 at Rs. 4.66 trillion.

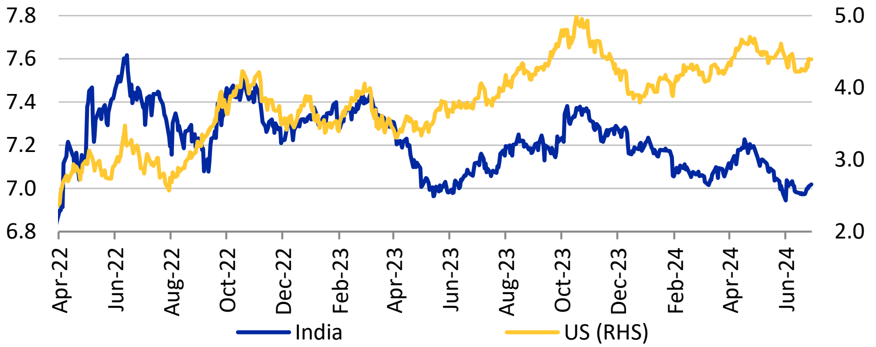
India's 10Y G-sec yield at 7.0%, post bond index inclusion; likely to trade with softening bias in the range of 6.80-7.15% in Q2 FY2025

EXHIBIT: Central government securities held by FPIs under Fully Accessible Route and General Investment Route



Source: CCIL; ICRA Research

EXHIBIT: India and US 10-year G-sec/Treasury yield



Source: Bloomberg; ICRA Research

- After witnessing an uptick in April 2024, India's 10-year G-sec (7.10 GS 2034) softened by 21 bps to 6.98% by the end-May 2024, over the levels seen at end-April 2024, benefitting from the downtrend in 10Y UST yield (to 4.50% by end-May 2024 from 4.68% by end-Apr 2024), as well as favourable domestic developments like reduction in planned T-bill issuances, buyback of G-secs and the large dividend pay-out by the RBI. On June 4, 2024 i.e. the day the Parliamentary election result was announced, the yield inched up to 7.04%. Thereafter, it eased to 6.97% on June 24, before rising to 7.01% by the month-end, tracking the movement in UST yield.
- Following the inclusion of IGBs in the J.P. Morgan Government Bond Index, India's 10Y G-sec yield has traded around 7.0% in recent sessions. The yield is likely to trade with softening bias, amid continued fiscal consolidation and the possibility of a cut in the budgeted market borrowings for FY2025.
- **ICRA expects the 10-year G-sec yield to trade between 6.80-7.15% in Q2 FY2025. Yields may harden close to the upper limit of this range, if the expectations about the timing of rate cuts by the MPC are pushed out beyond December 2024.**

ANNEXURE - I

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EXHIBIT: Centre's Gross Tax Revenues in FY2024 Prov., FY2025 IBE, and ICRA's projections for FY2025 RBE

Rs. Trillion	FY2024 Prov. (A)	FY2025 IBE (B)	FY2025 ICRA P (C)	Variation (C-B)	Growth (C)/(A)
Gross tax revenues~	**34.6**	**38.3**	**38.7**	**0.4**	**11.8%**
Direct taxes	**19.6**	**22.0**	**22.2**	**0.2**	**13.0%**
Corporation tax	9.1	10.4	10.3	-0.1	13.0%
Income tax*	10.5	11.6	11.9	0.3	13.0%
Indirect taxes	**13.6**	**14.7**	**14.9**	**0.2**	**9.5%**
CGST + IGST	8.2	9.2	9.2	0.0	11.8%
Customs Duty	2.3	2.3	2.4	0.1	5.0%
Union Excise Duty	3.05	3.18	3.21	0.02	5.0%
Compensation cess for GST	**1.4**	**1.5**	**1.5**	**0.0**	**6.1%**

*~Net of Refunds, Gross of States' share in Central Taxes; *Including other taxes such as fringe benefit tax, securities transaction tax, etc.; Prov.: Provisional Estimates; IBE: Interim Budget Estimates; RBE: Revised Budget Estimates; Source: GoI Budget Documents; CGA; ICRA Research*

ANNEXURE - II

EXHIBIT: Trends in key fiscal metrices and ICRA's projection for FY2025 RBE

Rs. Trillion	FY2024 Prov. (A)	FY2025 IBE (B)	FY2025 ICRA P (C)	Variation (C-B)	Growth (C)/(A)
Net Revenue Receipts	**27.3**	**30.0**	**31.2**	**1.2**	**14.5%**
Revenue Expenditure	**34.9**	**36.5**	**37.0 to 37.1**	**0.5 to 0.6**	**6.0% to 6.3%**
of which interest payments	10.6	11.9	12.0	0.1	12.8%
of which subsidies	4.1	3.8	3.8	0.0	-7.8%
Revenue Balance	**-7.7**	**-6.5**	**-5.8 to -5.9**	**0.7 to 0.6**	
As a % of GDP	**-2.6%**	**-2.0%**	**-1.8%**		
Disinvestment proceeds	0.2	0.5	0.5	0.0	191.6%
Capital expenditure, net lending	9.2	10.8	10.8	0.0	17.5%
Fiscal Balance	**-16.5**	**-16.9**	**-16.1 to -16.2**	**0.7 to 0.6**	
As a % of GDP	**-5.6%**	**-5.1%**	**-4.9% to -5.0%**		

Source: GoI Budget Documents; CGA; ICRA Research

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Analytical Contact Details

Name	Designation	Email	Contact Number
Aditi Nayar	Chief Economist, and Head - Research and Outreach	aditin@icraindia.com	0124- 4545 385
Rahul Agrawal	Senior Economist	rahul.agrawal@icraindia.com	022 – 6114 3425
Aarzoo Pahwa	Economist	aarzoo.pahwa@icraindia.com	0124 – 4545 835
Tiasha Chakraborty	Senior Associate Economist	tiasha.chakraborty@icraindia.com	0124- 4545 848
Isha Sinha	Associate Economist	isha.sinha@icraindia.com	022 – 6114 3445

Business Development/Media Contact Details

Name	Designation	Email	Contact Number
L Shivakumar	Chief Business Officer	shivakumar@icraindia.com	022-61693304
Neha Agarwal	Head – Research Sales	neha.agarwal@icraindia.com	022-61693338
Rohit Gupta	Head Business Development – Infrastructure Sector	rohitg@icraindia.com	0124-4545340
Vivek Bhalla	Head Business Development – Financial Sector	vivek.bhalla@icraindia.com	022-61693372
Vinita Baid	Head Business Development – Corporate Sector - West & East	vinita.baid@icraindia.com	033-71501131
Shivam Bhatia	Head Business Development – Corporate Sector - North & South	shivam.bhatia@icraindia.com	0124-4545803
Naznin Prodhani	Head – Group Corporate Communications & Media Relations	communications@icraindia.com	0124-4545860

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